



Ontario  
Securities  
Commission

Commission des  
valeurs mobilières  
de l'Ontario

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**IN THE MATTER OF THE *SECURITIES ACT*,  
R.S.O. 1990, c. S.5, AS AMENDED**

**- AND -**

**IN THE MATTER OF  
GROUND WEALTH INC., MICHELLE DUNK, ADRION SMITH, JOEL WEBSTER,  
DOUGLAS DEBOER, ARMADILLO ENERGY INC., ARMADILLO ENERGY, INC.,  
AND ARMADILLO ENERGY, LLC (aka ARMADILLO ENERGY LLC)**

**REASONS AND DECISION  
(sections 127 and 127.1)**

**Hearing:** In writing

**Decision:** August 24, 2015

**Panel:** Christopher Portner - Commissioner

**Submissions:** Jonathon T. Feasby - For Staff of the Commission  
Malinda N. Norman

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## REASONS AND DECISION

### I. OVERVIEW

- [1] This is a hearing before the Ontario Securities Commission (the “**Commission**”) pursuant to sections 127 and 127.1 of the *Securities Act*, R.S.O. 1990, c. S.5, as amended (the “**Act**”) to determine whether it is in the public interest to make an Order against Armadillo Energy Inc. (“**Armadillo Texas**”), Armadillo Energy, Inc. (“**Armadillo Nevada**”) and Armadillo Energy, LLC, also known as Armadillo Energy LLC (“**Armadillo Oklahoma**” and, collectively with Armadillo Texas and Armadillo Nevada, the “**Respondents**”).
- [2] The proceeding arose from a Notice of Hearing issued by the Commission on February 1, 2013, as amended on October 31, 2013, and a Statement of Allegations filed by Staff of the Commission (“**Staff**”) on February 1, 2013, as amended on October 31, 2013 (the “**Amended Statement of Allegations**”).
- [3] In the Amended Statement of Allegations, Staff alleges that, from October 2010 through April 2011 the (“**Material Time**”), the Respondents, together with Ground Wealth Inc. (“**GWI**”), Michelle Dunk, Adrion Smith, Joel Webster and Douglas DeBoer (collectively, the “**Settling Respondents**”) traded securities without being registered to do so and illegally distributed securities to Ontario investors. The securities entitled investors to the proceeds derived from the extraction and sale of oil that was subject to oil leases located in the State of Oklahoma, in the United States of America (the “**Armadillo Securities**”). Approximately CDN\$5,061,979 and US\$319,567 was raised from distributing the Armadillo Securities to more than 130 Canadian investors. Of this amount, approximately CDN\$2.8 million was raised from 68 investors who were Ontario residents.
- [4] All of the Settling Respondents have entered into settlement agreements which have been approved by the Commission and, as a result, are no longer parties to this proceeding.
- [5] The hearing on the merits in this proceeding was converted to a hearing in writing by Order of the Commission dated January 7, 2015.
- [6] The Respondents have not appeared or made submissions, and have not objected to the hearing on the merits being determined on the basis of the written record.
- [7] Pursuant to subsection 7(2) of the *Statutory Powers Procedure Act*, R.S.O. c. S. 22, the Commission has jurisdiction to proceed with a hearing in the absence of the Respondents when they have been given notice but have not appeared. I am satisfied that the Respondents have either been given notice or, in the case of Armadillo Oklahoma, that notice was waived by Order of the Commission dated July 8, 2014.
- [8] The written record which I have reviewed is comprised of the Affidavit of Stephen Carpenter, sworn May 15, 2014 (the “**Carpenter Affidavit**”), together with six volumes of exhibits to which the Carpenter Affidavit relates, and the Affidavit of Stephen Carpenter, sworn January 26, 2015 (the “**Carpenter Supplementary Affidavit**”), together with a seventh volume of exhibits to which the Carpenter Supplementary Affidavit relates.

[9] Although the Respondents are separate corporations, they operated as a single business entity in distributing the Armadillo Securities to investors, and in paying the financial obligations arising from those securities. The funds obtained from the investors were intermingled despite the fact that Armadillo Texas was the nominal issuer of the Armadillo Securities (Carpenter Affidavit, paras 32, 58, 172-177).

## **II. ISSUES**

[10] The issues that I must address are as follows:

- (a) Were the Armadillo Securities “securities” within the meaning of the Act?
- (b) Did the Respondents engage in unregistered trading contrary to subsection 25(1) of the Act?
- (c) Did the Respondents engage in an illegal distribution of securities contrary to subsection 53(1) of the Act?
- (d) Does the Commission have jurisdiction over the Respondents?

## **III. ANALYSIS**

### **A. Were the Armadillo Securities “securities” within the meaning of the Act**

[11] The following documents and instruments are included in the definition of “security” in subsection 1(1) of the Act:

(b) any document constituting evidence of title to or interest in the capital, assets, property, profits, earnings or royalties of any person or company,

...

(j) any certificate of interest in an oil, natural gas or mining lease, claim or relative voting trust certificate,

(k) any oil or natural gas royalties or leases or fractional or other interest therein,

...

(n) any investment contract.

[12] The term “investment contract” is not defined in the Act. The leading Canadian case relating to the interpretation of the term is *Pacific Coast Coin Exchange of Canada v. Ontario Securities Commission* (1978), 2 S.C.R. 112, in which the Supreme Court of Canada held (at pages 128-129) that an investment contract involves:

- (a) the advancement of money by an investor;
- (b) with an intention or expectation of profit;
- (c) in a common enterprise, in which the fortunes of the investor are interwoven with and dependent upon the efforts and success of those who solicit the capital (the promoters) or third parties; and

- (d) the efforts made by those other than the investor are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise.

[13] I find that the Armadillo Securities satisfy each of the criteria for an investment contract set out in paragraph [11] above and were securities within the meaning of the Act for the following reasons:

- (a) A total of CDN\$5,061,979 and US\$319,567 was invested in Armadillo Securities by investors (Carpenter Affidavit, paras. 172-175);
- (b) Investors who purchased Armadillo Securities did so with the expectation of a profit on their investment (Volume 1 of Exhibits to Carpenter Affidavit, Tabs 2D - GWI Brochure, 2E - Form of Partnership Agreement, and 2F - GWI/Armadillo Corporate Review); and
- (c) The Respondents were dependent on the investors for funds and the investors were dependent on the efforts and success of the Respondents and others, whose efforts were essential to the failure or success of the investment (Volume 1 of Exhibits to Carpenter Affidavit, Tabs 2E -Form of Partnership Agreement, and 2F - GWI/Armadillo Corporate Review).

[14] As the Armadillo Securities could be characterized as (i) documents constituting evidence of title to or an interest in the assets, property or earnings of a company; (ii) certificates evidencing an interest in oil; and/or (iii) oil royalties or leases or fractional or other interest therein, I also find that the Armadillo Securities are securities within the meaning of paragraphs (b), (j) and (k) of the definition of “security” in subsection 1(1) of the Act.

**B. Unregistered trading**

[15] Subsection 25(1) of the Act prohibits trading in securities by a person or company who is not registered as follows:

Unless a person or company is exempt under Ontario securities law from the requirement to comply with this subsection, the person or company shall not engage in or hold himself, herself or itself out as engaging in the business of trading in securities unless the person or company,

- (a) is registered in accordance with Ontario securities law as a dealer; or
- (b) is a representative registered in accordance with Ontario securities law as a dealing representative of a registered dealer and is acting on behalf of the registered dealer.

[16] The terms “trade” and “trading are defined in subsection 1(1) of the Act to include:

- (a) any sale or disposition of a security for valuable consideration....

...

(e) any act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance of any of the foregoing.

[17] In determining whether a respondent has engaged in acts in furtherance of a trade, the Commission has adopted a contextual approach which “requires an examination of the totality of the conduct and the setting in which the acts have occurred, the primary consideration of which is the effects the acts had on those to whom they were directed” (*Re Momentas Corp.* (2006), 29 OSCB 7408 (“*Momentas*”), at para. 77).

[18] A total of CDN\$5,061,979 and US\$319,597 of Armadillo Securities were sold to more than 130 investors (Carpenter Affidavit, paras. 114, 172; Volume 1 of Exhibits to Carpenter Affidavit, Tab 3A – Investor List). I find that the following conduct by the Respondents were acts in furtherance of the trades in Armadillo Securities:

- (a) Issuing the Armadillo Securities and working with GWI to market and sell those securities to Ontario investors (Exhibits to Carpenter Affidavits, Volume 1, Tabs 2E - Form of Partnership Agreement, 2F - GWI/Armadillo Corporate Review and Volume 2, Tab 1 - Excerpts of compelled interview of Michelle Dunk);
- (b) Accepting funds from the sale of Armadillo Securities to investors (Carpenter Affidavit, paras. 167-168, 172-175);
- (c) Making payments to investors in respect of the Armadillo Securities (Carpenter Affidavit, paras. 32, 75; Volume 2 of Exhibits to Carpenter Affidavit, Tab 1 - Excerpts of compelled interview of Michelle Dunk));
- (d) Providing promotional materials and forms of agreement to GWI to be provided to prospective investors (Carpenter Affidavit, para. 123; Volume 2 of Exhibits to Carpenter Affidavit, Tab 4 – Excerpts of compelled interview of Joel Webster);
- (e) Issuing ownership certificates and providing them to GWI to provide to investors (Carpenter Affidavit, para. 120);
- (f) Issuing and signing forms of agreement with investors (Carpenter Affidavit, paras. 144-146); and
- (g) Meeting with prospective investors for the purpose of marketing the Armadillo Securities (Carpenter Affidavit, paras. 132-134).

*Re Limelight Entertainment Inc.* (2008), 31 OSCB 1727 at paras. 131-133; *Momentas* at para. 80; *Re Lett* (2004), 27 OSCB 3215 at paras. 48-51, 64, aff'd, [2006] OJ No 751 (Div. Ct).

[19] During the Material Time, none of the Respondents and the Settling Respondents was registered to trade in securities (Volume 5 of Exhibits to Carpenter Affidavit, Tab 2 - Certificates).

[20] There is no evidence before me that the trades of Armadillo Securities were made pursuant to an exemption from the registration requirement.

[21] Based on the foregoing, I find that the Respondents engaged in unregistered trading contrary to subsection 25(1) of the Act.

**C. Illegal distribution of securities**

[22] Subsection 53(1) of the Act prohibits the distribution of securities without a prospectus as follows:

No person or company shall trade in a security on his, her or its own account or on behalf of any other person or company if the trade would be a distribution of the security, unless a preliminary prospectus and a prospectus have been filed and receipts have been issued for them by the Director.

[23] A distribution, where used in relation to trading in securities, is defined in subsection 1(1) of the Act to mean “a trade in securities of an issuer that have not been previously issued.”

[24] As discussed above, the Respondents traded Armadillo Securities. Those trades were a distribution as the Armadillo Securities had not been previously issued (Volume 1 of Exhibits to Carpenter Affidavit, Tab 2E - Form of Partnership Agreement, Tab 2F - GWI/Armadillo Corporate Review).

[25] The evidence establishes that neither a preliminary prospectus nor a prospectus for the Armadillo Securities was filed with the Commission (Volume 5 of Exhibits to Carpenter Affidavit, Tab 2 - Certificates).

[26] Based on the foregoing, I find that the Respondents distributed Armadillo Securities contrary to subsection 53(1) of the Act.

**D. Does the Commission have jurisdiction over the Respondents?**

[27] Having found above that the Respondents engaged in unregistered trading contrary to subsection 25(1) of the Act, I must determine whether the Respondents traded securities in Ontario. It is sufficient for the foregoing purpose if a person engages in Ontario in any acts in furtherance of a trade in a security (*Re Lehman Brothers & Associates Corp* (2011), 34 OSCB 12717 at paras. 35-37).

[28] There were numerous acts by the Respondents in furtherance of trading in the Armadillo Securities including the following:

- (a) The Respondents, working with GWI, distributed the Armadillo Securities to residents of Ontario (Carpenter Affidavit, para. 114);
- (b) Funds from the distribution of Armadillo Securities were deposited to bank accounts in Ontario (Carpenter Affidavit, para. 167);
- (c) Funds collected from the distribution of Armadillo Securities in Ontario were used to fund GWI in Ontario and were distributed to the Respondents (Carpenter Affidavit, paras. 167-173); and
- (d) The Respondents sent cheques to GWI in Ontario for distribution to Ontario investors and transferred funds directly to the bank accounts of Ontario investors (Carpenter Affidavit, paras. 167, 176).

[29] Based on the foregoing, I find that the Commission does have jurisdiction over the Respondents for the purposes of this proceeding.

#### **IV. CONCLUSION**

[30] I find that, during the Material Time, the Respondents traded Armadillo Securities without registration and distributed Armadillo Securities without a prospectus contrary to subsections 25(1) and 53(1) of the Act and contrary to the public interest.

[31] An order will be issued as of the date of these Reasons and Decision as follows:

- (a) The Respondents have until September 2, 2015 to notify the Secretary of the Commission that they, or any of them, require an oral sanctions hearing, which, if required, will then be scheduled by the Secretary;
- (b) Failing notification by the Respondents, Staff shall serve and file their written submissions on sanctions and costs by September 11, 2015;
- (c) The Respondents shall serve and file their written submissions on sanctions and costs by September 18, 2015; and
- (d) Staff shall serve and file reply submissions on sanctions and costs, if any, by September 25, 2015.

Dated at Toronto this 24<sup>th</sup> day of August, 2015.

*“Christopher Portner”*

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Christopher Portner